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C O N F I D E N T I A L SECTION 01 OF 03 BAGHDAD 001481

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SUBJECT: TRADE MINISTRY SEEKS BILLIONS TO FUND PDS IN 2008  
AND REFORM IT IN 2009

REF: A. BAGHDAD 1421

[1](#)B. BAGHDAD 789

[1](#)C. BAGHDAD 95

Classified By: Economic Counselor Todd P. Schwartz for reasons 1.4 (b)  
and (d).

[1](#)1. (C) SUMMARY: Deputy Minister of Trade Abdul Hadi Kadhim al Hameiri told Emboffs that the Ministry of Trade (MinTrade) needs USD 4 to 4.5 billion to fund the Public Distribution System (PDS) for the remainder of 2008; increased commodities and shipping costs will consume MinTrade's roughly USD 3.3 billion 2008 budget allocation by the end of June. Abdul Hadi was cautiously optimistic that the Council of Ministers (CoM) and the Council of Representatives (CoR) would approve MinTrade's supplemental request. (NOTE: Finance Minister Bayan Jabr recently told us MinTrade would receive no more than USD 1 to 2 billion in 2008 supplemental appropriations for the PDS (reftel A). END NOTE.) Abdul Hadi was also guardedly sanguine about MinTrade's plans to means-test PDS beneficiaries and monetize their benefits beginning in 2009 (reftel B); he noted that the High Economic Committee (HEC) and the Prime Minister's Office (PMO) have approved the reform roadmap but that increasing public concerns about food security would challenge implementation efforts. He said MinTrade would need USD 10 to 10.5 billion to carry out its reform plans in 2009 but that, if the plans unfolded as envisioned, PDS costs would fall significantly in 2010 and thereafter. He agreed with Emboffs that MinTrade would need a strong public relations campaign to educate PDS beneficiaries, as well as private sector food importers, distributors, and retailers, so that they understood their respective roles under the reform agenda. MinTrade appears on track to implement PDS reforms in 2009, but significant political challenges lie ahead. The GOI should be encouraged to move forward on this International Compact with Iraq (ICI) benchmark with important ramifications for Iraq's fiscal, economic, and political wellbeing. END SUMMARY.

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UNFUNDED MANDATE: HIGH FOOD PRICES HIT MINTRADE'S BUDGET  
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[1](#)2. (C) Abdul Hadi told Emboffs that MinTrade needs USD 4 to 4.5 billion to fund the PDS for the remainder of 2008. He complained that the Ministry had been strapped with an unfunded mandate: during negotiations over the 2008 budget, the CoM and the CoR rejected MinTrade proposals to eliminate some PDS benefits and beneficiaries (reftel C) but then merely straight-lined the 2007 budget PDS allocation for this year, taking no account of rising global commodities and shipping prices. Abdul Hadi said FinMin Jabr had assured him then that MinTrade would receive adequate mid-year supplemental appropriations for the PDS, but Jabr was now proving stingier. (NOTE: Article 27 of the FY2008 budget legislation confusingly mandates that MinTrade provide the whole PDS basket of goods and fund the program fully, including through supplemental appropriations, but provides

no concomitant instructions to the Finance Ministry to provide the additional funding. END NOTE.) Abdul Hadi told us that MinTrade recently presented the HEC with a report justifying its supplemental budget request and claimed there was "consensus" among HEC members that the appropriation is necessary. MinTrade contracts for PDS supplies through June 2008 totaled roughly USD 3.6 billion, putting the program's current supply situation in good stead but its finances in the red. Abdul Hadi said he implored the HEC to fund the PDS fully, given high food prices and the potential for political backlash if rations were cut.

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MOVING DOWN THE PDS REFORM ROADMAP  
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¶3. (C) Abdul Hadi said MinTrade's plans to begin means-testing PDS beneficiaries and monetizing benefits in 2009 are moving forward. He said the HEC and the PMO have approved the plans; he was unsure, however, whether the CoM would submit the proposal to the CoR for approval. He told us Deputy CoR Speaker Sheikh Khalid Attiyah also supports the plan and has instructed the CoR Economic Committee to study the roadmap.

¶4. (C) MinTrade has developed the income declaration form it intends to use to identify and document eligible beneficiaries and has stipulated a monetary penalty for falsifying information on it. Abdul Hadi said the Ministry would initially establish an income threshold that would entitle roughly 75 percent of Iraqis to PDS benefits. (NOTE: Virtually all Iraqis presently qualify for PDS benefits. END

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NOTE.) He told us MinTrade would use the income declaration form for the 2008 registration period (generally in November of the current year for the following year's benefits) and update the rolls by year end 2008. He noted that the Interior Ministry's national identification "smart card," which MinTrade had planned to use as a stored-value card to distribute monetized PDS benefits, would not be ready by next year. MinTrade therefore would instead circulate the new beneficiary rolls to regional branches of state-owned and private banks nationwide, where next year's PDS beneficiaries would proceed to receive their payments in cash.

¶5. (C) COMMENT: This adjustment to the reform plans Abdul Hadi had briefed to us (reftel B) has potential upside and downside risks. No longer reliant on new technology that would have required substantial resources to roll out, operate, and maintain, MinTrade's reform plans should be easier to implement by next year. Cash benefits would also be more liquid than stored value on a smart card, giving PDS beneficiaries greater freedom as consumers. Using state-owned and private banks as conduits should also further development of the retail banking sector. At the same time, using cash will present challenges. Injecting trillions of Iraqi Dinars into the economy could put pressure on inflation, which the Central Bank of Iraq (CBI) has worked diligently--and, so far, successfully--to keep in check. Moreover, moving more truckloads of cash around the country will increase the opportunities for insurgents and militias to interdict and misappropriate them. Monetizing PDS benefits with cash--as opposed to vouchers, coupons, or a stored-value smart card--will require MinTrade to coordinate closely with Iraq's fiscal and monetary policymakers as well as the security forces. END COMMENT.

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A USD 10 BILLION ONE-OFF FOR PDS IN 2009  
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¶6. (C) Abdul-Hadi said MinTrade would need USD 10 billion to fund the PDS reform plans in 2009 but that the program's costs should fall significantly by 2010 if the plans unfolded as envisaged. As reported in reftel B, in 2009 MinTrade

plans to distribute monetized benefits to the means-tested list of beneficiaries, empowering them to purchase their estimated demand for PDS commodities at prices reflecting the total cost of importation and distribution, plus a 15 to 20 percent profit (the figure remains to be determined) for the retailers. In addition, MinTrade intends to procure and distribute through its existing state-owned channels 50 percent of the program's total forecast demand--opening the door for the private sector to import and distribute the other 50 percent, presumably more efficiently and at better prices. MinTrade will provide the goods it procures to PDS food agents on contract, obligating the agents to remit to the Ministry the revenues from the retail sale of these items, less the agents' pre-agreed 15 to 20 percent profit.

17. (C) In 2009 MinTrade's initial cost for funding the PDS will therefore be more than 150 percent of the retail cost of goods to supply the program. Abdul Hadi forecasts that MinTrade would need roughly USD 6 billion to empower the means-tested beneficiaries to purchase their basic needs and another USD 4 to 4.5 billion for the Ministry to supply retailers with 50 percent of the goods to meet those needs. As the beneficiaries purchased MinTrade-supplied goods at their local food agents, however, the agents would remit back to the Ministry much of its upfront outlays. By 2010, MinTrade intends to purchase only 25 percent of the program's needs, allowing the private sector to supply the other 75 percent; Abdul Hadi thought the 2009 food agents' remittances would fund much of the program in 2010.

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EDUCATING THE PUBLIC WILL BE ESSENTIAL  
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18. (C) Abdul Hadi agreed with Emboffs that MinTrade will need an effective public education campaign to advise PDS beneficiaries, as well as private sector food importers, distributors, and retailers of the challenges and opportunities the reforms will present in 2009. Emboffs queried whether the Ministry had the expertise needed to launch such a campaign and suggested MinTrade contract a private public relations firm to assist them. Abdul Hadi seemed receptive to the idea. He hoped the Ministry would begin educating the public by mid-year, once the HEC had approved the income threshold and the amount of monetized benefit to be awarded, giving all concerned a full six months of lead time. Emboffs observed and Abdul Hadi agreed that the public education campaign should also reach Iraqi farmers

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before the late-summer planting season, so that they could make informed decisions about what to plant and whether to sell their harvest to MinTrade or to private sector PDS suppliers. Emboffs also noted that MinTrade would need a robust private sector price tracking capability so that MinTrade could adjust its own prices for PDS goods periodically during the year.

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COMMENT  
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19. (C) Abdul Hadi said repeatedly that MinTrade's goal with its reform roadmap is to "get out of the business" of the PDS. While clearly proud of his team's efforts to create the reform plans, which also enjoy support from the World Bank, he soberly assessed that significant political challenges lie ahead. He opined that many of his colleagues in government and the CoR "have no patience" for multi-step, medium-term approaches to problem solving, preferring instead "quick fixes" that do nothing to address the heart of the matter; he put proposals to cut PDS rations and prosecute fraudsters in this latter category. "This is about economic reform," he stressed. He observed that food security fears in the current climate of high international commodities prices could weaken the resolve of GOI leaders who until now have

supported MinTrade's plan. Though it has its shortcomings, MinTrade's roadmap remains the most viable alternative, presently enjoying high-level GOI support, for achieving this important ICI benchmark over the next two years. The GOI should be encouraged to fund the PDS adequately this year to forestall potential social and political unrest that could result if ordinary Iraqis felt more acutely the strain of high international food prices. The GOI should further be encouraged and assisted to continue implementing MinTrade's roadmap.

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